

15. For these reasons, simple pledges by BellSouth that it "has been" or that it "will be" in compliance with section 272 should be given no weight. Rather, BellSouth must be called upon to come forward with specific, concrete evidence that shows, among other things:

- that all BellSouth/BSLD transactions, whether involving assets, information, or services, and including "chain transactions" involving a separate nonregulated affiliate,<sup>8</sup> have been reduced to writing and made available for public inspection;
- that all BellSouth/BSLD transactions (again including "chain transactions") to date have been conducted on an "arm's length" basis and have been nondiscriminatory;
- that detailed internal accounting and tracking systems are in place and operational so as to comply with the Accounting and Non-Accounting Safeguards Orders and with section 272;
- that internal oversight procedures are in place to ensure that all affiliate transactions are conducted on an "arm's length" basis and are non-discriminatory;
- that asset allocations required by the Accounting Safeguards Order have been fairly established;
- that methods of valuing transactions between BellSouth and BSLD meet Commission guidelines (such as the derivation of the "fully distributed costs" that BellSouth repeatedly references in its general descriptions of services provided to BSLD) and have been fairly and accurately established;
- that the transactions between BellSouth and BSLD have not, and do not, provide impermissible cross-subsidization of BSLD; and
- that, as discriminatory conduct and cross-subsidization may already have occurred, BellSouth and BSLD must have procedures in place to

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<sup>8</sup> The Commission repeatedly has made clear that the affiliate transaction rules govern "chain transactions" where an unregulated affiliate stands between the BOC and the section 272 in the provision of assets, information, or services. See Accounting Safeguards Order, ¶¶ 183, 251; Non-Accounting Safeguards Order, ¶ 309; Ameritech Michigan Order, ¶ 373.

"true-up" these past transactions so that BSLD does not enter the interLATA market with unlawful pre-authorization subsidies or other unlawful advantages from BellSouth.

16. The evidence that BellSouth must be required to present should include, among other things, the following, all of which are readily available to BellSouth:

- financial reports of BellSouth and BSLD;
- specific terms and conditions of asset transfers and other transactions between BellSouth and BSLD, including transfers, sales and/or leases of property, equipment, and information, and employee transfers;
- the specific terms and conditions of service transactions conducted between BellSouth and BSLD;
- the precise extent to which the affiliate has used the services of BellSouth employees in the planning, construction, or maintenance of BSLD's network and how such services were accounted for; and
- the specific nature and extent of funding of BSLD.

17. The absence of these types of specific evidence, without any justifying explanation, should raise immediate doubts as to whether a BOC and its section 272 affiliate have in fact operated in compliance with section 272. A BOC cannot hope to meet its burden under section 271(d)(3) without such a presentation.

18. As I discuss more fully below, BellSouth's application fails to present the type of detailed, concrete evidence necessary to make any meaningful evaluation of its assertions that it will comply with section 272. Indeed, BellSouth repeatedly states its disagreement with the Commission regarding its obligations under section 272, stating that it is under no current obligation to ensure that its transactions with BSLD are publicly disclosed, are arm's length in nature, or otherwise comply with section 272 prior to being

granted interLATA authority.<sup>9</sup> In addition, BellSouth also states that it intends to follow the same marketing practices found unacceptable in the Ameritech Michigan Order.

**IV. BELLSOUTH CURRENTLY IS NOT IN COMPLIANCE WITH THE DISCLOSURE REQUIREMENTS OF SECTION 272(b)(5).**

**A. The Written Descriptions Of The Types Of Services Provided By BellSouth To BSLD Do Not Satisfy The Requirement That Each Transaction Be "Reduced To Writing."**

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19. Section 272(b)(5) requires that each transaction between BellSouth and its section 272 affiliate BSLD be "reduced to writing and available for public inspection." In the Accounting Safeguards Order, the Commission determined that this "reduced to writing" requirement meant "that the description of the asset or service and the terms and conditions of the transaction should be sufficiently detailed to allow us to evaluate compliance with our accounting rules." Accounting Safeguards Order, ¶ 122. In the Ameritech Michigan Order, the Commission made clear that such descriptions must "disclose the actual rates for [the BOC's] transactions with its section 272 affiliate." Ameritech Michigan Order, ¶ 369.

20. These public disclosure requirements are critical to enabling CLECs, IXC's, and the Commission to assess, among other things, (i) whether the BOC is impermissibly subsidizing the section 272 affiliate, and (ii) whether the BOC is

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<sup>9</sup> Even BellSouth concedes, however, that current compliance is "highly relevant" as evidence of future compliance if the BOC claims that it is currently in compliance. BellSouth Br. at 59. Therefore, even under BellSouth's own argument, its failure to reduce all transactions between BellSouth and BSLD to writing and post these transactions for public inspection is "highly relevant," because BellSouth does, in fact, claim that it complies with section 272. See Affidavit of Guy L. Cochran, in the Matter of Application by BellSouth Corporation for Provision of In-Region, InterLATA Services in South Carolina ("Cochran Aff."), ¶¶ 8, 11, 23; Varner Aff., ¶¶ 204, 210, 212, 214, 217-18, 220, 222. In any event, the fact that BellSouth seeks reconsideration of the Ameritech Michigan Order does not exempt it from complying with the Commission's orders during the pendency of its petition. See 47 U.S.C. § 405.

impermissibly engaging in transactions with its section 272 affiliate with terms, conditions, or arrangements that are more favorable than those offered to CLECs or to IXC's.

Furthermore, the information disclosed must be "detailed" and sufficient "to allow [the Commission] to evaluate compliance with [its] accounting rules." Accounting Safeguards Order, ¶ 122. Obviously, a simple disclosure that certain types of transactions occurred and the general subject matter of those transactions is insufficient. See Ameritech Michigan Order, ¶ 367.

21. The meager information BellSouth has disclosed concerning its many transactions with BSLD clearly does not comply with section 272(b)(5) and the Accounting Safeguards Order. The only information concerning past and ongoing transactions between BellSouth and BSLD presented in this section 271 application is contained in the affidavit of Victor E. Jarvis. That affidavit does not provide descriptions of individual transactions, but rather broadly identifies 15 categories of services that BellSouth has provided to BSLD, such as "Customer Billing Services," "Project Management," "Collocation," and "Mail Service." Jarvis Aff. at 6-10. Not one of the descriptions provided under these service category headings includes prices, rates, or other terms and conditions for any particular transaction. Instead, each description of a service category provides only a total cost figure for all the transactions grouped under that category.<sup>10</sup> For example, the "Information Technology - Billing Systems" category states that BellSouth has provided BSLD "services associated with the development, design, coding, and testing of systems," and "the amount for these services totaled \$2,859,900." Jarvis Aff. at 8. BellSouth does not provide specific descriptions of

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<sup>10</sup> According to BellSouth, the costs of these fifteen categories of services for BSLD total over \$8.8 million. Jarvis Aff. at 6-10.

the goods and services rendered, it does not provide any contract terms, and it does not even identify the dates or time periods during which these various services were performed.

22. Moreover, although BellSouth states that its application includes a "description of all transactions between [BellSouth] and BSLD to date," BellSouth Br. at 59, the description of services in the Jarvis affidavit on its face does not disclose all the transactions between BellSouth and BSLD. The Jarvis affidavit states that the service descriptions are limited to services only "through July 31, 1997." Jarvis Aff. at 6. BellSouth's failure to provide any description of all transactions occurring after July 31, 1997, is a direct violation of the Commission's Ameritech Michigan Order. See Ameritech Michigan Order, ¶ 370. BellSouth has given no explanation for this apparently arbitrary cut-off date.

23. BellSouth does not discuss whether any written agreements have been entered into between BellSouth and BSLD concerning these different services. If written agreements exist, they must be disclosed by BellSouth before any judgment can be made as to the arm's length character of these transactions. If written agreements do not exist, the lack of written agreements is itself a violation of section 272. § 272(b)(5). Moreover, if no such written agreements exist for these transactions worth over \$8.8 million, that fact alone would be striking evidence that the transactions were not arm's length in character.<sup>11</sup>

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<sup>11</sup> BellSouth simply is not at liberty to conduct its dealings with BSLD on any basis other than through written agreements, and those agreements must be available for public inspection. Section 272(b)(5) requires that all "transactions" between a BOC and its affiliate must be "reduced to writing," while the Accounting Safeguards Order provides that a "transaction" exists "[o]nce the BOC and its affiliate have agreed upon the terms and conditions." Accounting Safeguards Order, ¶ 124.

24. BellSouth's repeated assertion that it provides services to BSLD at "fully distributed costs" is also inadequate to meet its burden of showing compliance with the applicable accounting rules. At a minimum, BellSouth must demonstrate what these "fully distributed costs" actually were and must include both rates and the terms and conditions for the services that BellSouth provided to BSLD. "[A] statement of the valuation method used, without the details of the actual rate" does not meet BellSouth's legal obligation under the Accounting Safeguards Order. Ameritech Michigan Order, ¶ 369 (emphasis added).

25. Not only are BellSouth's transaction disclosures too vague and lacking in detail to satisfy the "reduced to writing" requirement of section 272(b)(5), but at least one description regarding collocation arrangements between BellSouth and BSLD, appears on its face to be discriminatory. According to this description, BellSouth has "granted BSLD the right to occupy" collocation space in BellSouth end offices in four states. Jarvis Aff. at 10. Although the affidavit asserts, without supporting information or data, that the spaces were leased at "prevailing company price[s]," it notes that these collocation rights are "granted for a period of two years from the date BSLD's equipment becomes operational." Id. This collocation arrangement thus appears to grant BSLD an open-ended guarantee that collocation space will be available to it whenever it becomes operational. Such a guarantee would provide preferential treatment for BSLD over other carriers which face an SGAT that states "BellSouth assigns space for collocation based on space availability and on a first come, first serve basis." Varner Aff., Exhibit AJV-4 at 9 (BellSouth Collocation Handbook).

B. BellSouth Has Violated The Requirements Of The Statute And The Accounting Safeguards Order By Failing To Make Transactions Between BellSouth and BSLD "Available For Public Inspection."

26. As noted above, section 272(b)(5) requires that "all transactions" between a BOC and its section 272 affiliate not only be "reduced to writing," but also be "available for public inspection." In the Ameritech Michigan Order, the Commission found that these disclosure requirements took effect on passage of the Act on February 8, 1996, and that, since that time, BOCs and their section 272 affiliates have been required to make publicly available all transactions for information, services, or facilities in which they have been engaged. Ameritech Michigan Order, ¶ 371.

27. The Accounting Safeguards Order held that section 272(b)(5)'s public disclosure obligation requires affiliates, "at a minimum, to provide a detailed written description of the asset or service transferred and the terms and conditions of the transaction on the Internet within 10 days of the transaction through the company's home page." Accounting Safeguards Order, ¶ 122. The Accounting Safeguards Order's public disclosure obligations became effective on August 12, 1997. See Accounting Safeguard Rule Changes Requiring OMB Approval Soon to be Effective, Public Notice, DA 97-1669 (released Aug. 5, 1997).

28. BellSouth has been, and continues to be, in violation of disclosure requirements under section 272(b)(5) and the Accounting Safeguards Order. AT&T regularly has accessed the Internet home page for BellSouth to determine whether any transactions between BellSouth and BSLD have been posted as anticipated in the Accounting Safeguards Order. Until approximately October 1, 1997, BellSouth's home page contained no reference

to any transaction disclosures prompted by section 272. At the time of this section 271 application, BellSouth changed its home page to include a site that stated as follows:

"This index will contain a listing of those completed transactions between BellSouth Telecommunication, Inc. and BellSouth Long Distance, Inc. required to be posted on the internet by the [FCC] in CC Docket 96-150. Required posting will occur within 10 days of the transaction."<sup>12</sup>

To date, this Internet site has never contained a description of a single transaction between BellSouth and BSLD. Thus, although BellSouth states that "transactions that must be posted . . . will be forwarded . . . for appropriate inclusion to the Internet site," and suggests that the site is up and running, Jarvis Aff. at 10, BellSouth has never posted any information regarding any transactions with BSLD. Indeed, the site does not even include the general service descriptions provided in the Jarvis affidavit.

29. In an attempt to meet its burden of satisfying the public disclosure requirements under section 272(b)(5), BellSouth's section 271 application asserts without qualification that "[a]ll transactions between [BellSouth] and BSLD have been and will be conducted on an arms [sic] length basis, reduced to writing and made available for public inspection . . . . Written disclosure of these transactions is available for public inspection at BellSouth Center, 675 West Peachtree Street, NE, Atlanta, Georgia." Cochran Aff., ¶¶ 23, 26. Based on my own first-hand experience, this statement is false.

30. On October 6, 1997, I went to the BellSouth Center at 675 West Peachtree Street, NE, Atlanta, Georgia, as identified in the Cochran affidavit and asked to see all documents available for public inspection that were relevant to BellSouth's section 271 application. I was informed that I must send a request in writing for the documents I wished

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<sup>12</sup> A copy of this Internet site is attached to this affidavit as Attachment 1.



to view to Mr. Jim Llewellyn, an attorney for BellSouth whose name appears on the cover of the BellSouth section 271 application. I immediately faxed a letter to Mr. Llewellyn stating that AT&T wished to review the documents referenced in paragraphs 23 and 25 of the Cochran affidavit and that we would be returning to BellSouth Center the next morning unless we heard from BellSouth.<sup>13</sup>

31. When I arrived at the BellSouth Center the next morning, I was informed that no documents were available for public inspection until we spoke with Mr. Llewellyn. My counsel then called Mr. Llewellyn. My counsel explained that we wanted to see the documents that BellSouth's affiant said were available for public inspection. Mr. Llewellyn stated that he did not know what documents we wanted to review because he had not yet reviewed the fax that I had sent him the day before. Mr. Llewellyn also stated that we would not be allowed to review any documents until he had a chance to review our fax and the Cochran affidavit and had received proof of my counsel's identity. Mr. Llewellyn stated that he would contact us later.

32. Later that same day, Mr. Llewellyn called my office and spoke to my counsel. Mr. Llewellyn stated that there were currently no documents available for public inspection. Mr. Llewellyn explained that paragraph 23 was "inartfully drafted" because it was BellSouth's contention that the phrase "have been" in the statement: "All transactions between BST and BSLD have been and will be conducted on an arms length basis, reduced to writing and made available for public inspection,"<sup>14</sup> modifies only the phrase "conducted on arm's length basis," and does not modify the phrase "available for public inspection."

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<sup>13</sup> A copy of this letter is attached as Attachment 2 to this affidavit.

<sup>14</sup> Cochran Aff., ¶ 23.

33. After hearing this explanation for why no documents were available for public inspection, my counsel pointed out to Mr. Llewellyn paragraph 26 of the same affidavit which stated, in the present tense: "Written disclosure of these transactions is available for public inspection at BellSouth Center." Mr. Llewellyn then stated that he did not know to what transactions that paragraph was referring, and questioned whether this paragraph may have also been "inartfully drafted." Mr. Llewellyn asked for additional time to look into this matter.

34. At approximately noon on the next day, October 8, 1997, Mr. Llewellyn called to state that documents were now in fact available for inspection by AT&T. On review, AT&T representatives discovered that these documents consisted of a listing of the 5 categories of services that BellSouth anticipated it would provide to BSLD in the future and a listing of 15 other categories of services that BellSouth already had provided to BSLD. The descriptions essentially parroted the same descriptions that are found in the Jarvis affidavit, although, unlike the Jarvis affidavit descriptions, they did not contain any aggregate cost information. Each service description was placed on a separate page, for a total of twenty pages. Moreover, BellSouth did not produce a certified statement from an officer of BellSouth concerning these transactions, as required by the Accounting Safeguards Order. See Accounting Safeguards Order, ¶ 122.

35. Thus, despite claiming in its application that written descriptions for all its transactions with BSLD were available for public inspection, BellSouth first told AT&T that no such records were available for review, then begrudgingly produced a meager listing describing categories of services provided to BSLD, rather than detailing each of the

transactions. This conduct plainly shows that BellSouth has not met its disclosure obligations under section 272(b)(5).

36. BellSouth has deliberately defied the Commission by failing to post any transactions on the Internet. Accounting Safeguards Order, ¶ 122. In addition, BellSouth has defied the Commission by failing to describe the transactions between BellSouth and BSLD with "sufficient[] detail to allow [the Commission] to evaluate compliance." Id. It also has defied the Commission by failing to have these transactions available for public inspection at its place of business. Id. Consequently, BellSouth has not come close to meeting its obligations under section 272 and the Accounting Safeguards Order.

**V. BELL SOUTH HAS NOT PRESENTED ANY TANGIBLE EVIDENCE THAT IT HAS PROCEDURES OR SYSTEMS IN PLACE TO PROTECT AGAINST VIOLATIONS OF SECTION 272.**

37. The Telecommunications Act has required BellSouth to change the way it does business. Section 272 itself presents a series of obligations that BellSouth must face, such as requiring it to create a wholly separate company to provide a telecommunications service that must operate independently of BellSouth, and that must not be provided services, information, or facilities on terms any more favorable than those provided to the competitors of BellSouth.

38. In the face of these types of significant changes in the way business must be done, basic accounting principles require that BellSouth create new internal systems and procedures to protect against violations of its new legal obligations. In particular, when organizations are undergoing major change, one of the most important internal controls is

risk assessment.<sup>15</sup> Although BellSouth promises compliance and coverage for BellSouth employees, it provides no support or documentation describing procedures that BellSouth has implemented in response to the changing risks due to BellSouth's 271 application.

BellSouth's business-as-usual attitude relies on its established control environment to provide internal discipline and structure. Because BellSouth has shown in its previous dealings with affiliates its ability to obstruct audits and benefit from delays inherent in the regulatory process, the Commission should be especially vigilant in regards to internal control.

39. For example, BellSouth's affidavits refer generally to internal audits that have been conducted (without identifying the specific purposes of these audits, the procedures followed, or their results), and appear to suggest that these internal audits will continue and will protect against violations of section 272. Cochran Aff., ¶ 22; Jarvis Aff. at 4. But for such internal audits to be effective in identifying violations of section 272, auditing procedures must be revised to include methods specifically designed to seek out and evaluate transactions for assets, services and information that were not recorded or subject to a written agreement. No reliable or accurate evaluation of section 272 compliance can be made without identifying (or confirming the non-existence of) unrecorded transactions, because it is just such unrecorded dealings that provide the most ready means by which BellSouth and BSLD could engage in unfair cross-subsidization or other anticompetitive activities. BellSouth provides no specific evidence to show that its auditing program has been revised to address the unique compliance issues raised by section 272.

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<sup>15</sup> "[R]isk assessment for financial reporting purposes is its identification, analysis, and management of risks relevant to the preparation of financial statements that are fairly presented in conformity with generally accepted accounting principles." AICPA Professional Standards, Statements on Auditing Standards, Vol. I., AU 319.28.

40. BellSouth has not identified any internal systems or procedures that it has instituted specifically to address the requirements of section 272 and to attempt to protect against violations of section 272. Indeed, BellSouth acknowledges that it has not even taken the preliminary step of conducting employee training on section 272 obligations,<sup>16</sup> despite the fact that its employees are actively engaged in providing substantial services and information to BSLD. Jarvis Aff. at 6-10. Without evidence of such systems or procedures, there is no basis to conclude that BellSouth is ready and able to comply with section 272. These systems and procedures must address the following compliance problems, among others, raised in the context of section 272:

- (i) BSLD's workforce includes a significant number of employees who formerly worked at BellSouth (although BellSouth is silent on the precise number of former BellSouth employees now at BSLD). These BSLD employees will have both the incentive and the ability to seek and obtain favorable treatment from their former coworkers at BellSouth, which obviously would be impermissible under section 272.
- (ii) BSLD and BellSouth employees will have an incentive to engage in "off-the-record" transactions, especially concerning proprietary information such as CPNI. Such "off-the-record" transactions will be especially difficult to identify and evaluate through any internal or external audit.

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<sup>16</sup> See Affidavit of George F. Agerton, in the Matter of Application by BellSouth Corporation for Provision of In-Region, InterLATA Services in South Carolina, ¶ 11. BellSouth presents some information on employee training it has conducted concerning its obligations under sections 251 and 252 of the Act. *Id.* at ¶¶ 6-10. The obligations under section 272, however, substantially differ from those arising under sections 251 and 252.

(iii) BSLD employees formerly employed by BellSouth have an incentive to take with them, and use, BellSouth proprietary information without accounting for this acquisition of information and without offering this information to competitors.

(iv) BSLD and BellSouth will have a strong incentive to share employee services on an ad hoc basis without properly accounting for such services.

41. The type of compliance programs instituted by other BOCs with which I am familiar include procedures requiring that all transactions between a BOC and its section 272 affiliate be reviewed by an oversight committee to confirm its compliance with section 272. In this way the BOC can separate the process of evaluating section 272 compliance from the employees who are most interested in seeing the transaction completed. In addition, at least one BOC has stated its intent to require that all transactions proceed through specified customer contact points, which can help to ensure that affiliates, CLECs, and IXC's each receive the same access to BOC facilities, information, and services, and which protects against ad hoc "off-the-record" transactions.

42. I view compliance programs such as these, which are specifically geared to the unique obligations posed by section 272, as a prerequisite for a BOC to establish that it is ready and able to comply with section 272. BellSouth's failure to present any tangible evidence of its implementation of such programs, despite having engaged in substantial ongoing transactions with BSLD, shows that it is not prepared to provide interLATA service in compliance with section 272.

**VI. BELLSOUTH'S PROPOSED TELEMARKETING FOR INBOUND CALLS IS VIRTUALLY IDENTICAL TO THE TELEMARKETING SCRIPT REJECTED IN THE AMERITECH MICHIGAN ORDER.**

43. BellSouth states that, once it begins offering BSLD long-distance service under a joint marketing agreement, it will instruct its customer service representatives to "advise that several companies provide long distance, recommend BSLD and offer to read from a list of available carriers." Varner Aff., ¶ 230. BellSouth has identified the following language as acceptable for its customer service representatives who receive inbound calls from customers requesting new service or a change in existing service:

"You have many companies to choose from to provide your long distance service. I can read from a list the companies available for selection, however, I'd like to recommend BellSouth Long Distance." Id.

BellSouth has stated, further, that its customer service representatives will read a list of available long distance carriers only "if the customer requests it to be read." Id. at ¶ 231.

44. In the Ameritech Michigan Order, the Commission held that the following suggested inbound telemarketing script "would violate the 'equal access' requirements of section 251(g):

"You have a choice of companies, including Ameritech Long Distance, for long distance service. Would you like me to read from a list of other available long distance companies or do you know which company you would like."

Ameritech Michigan Order, ¶¶ 375-76.

45. The anticipated telemarketing by BellSouth<sup>17</sup> thus is virtually identical

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<sup>17</sup> BellSouth contends that it "does not use verbatim scripts for such customer contacts." Varner Aff., ¶ 230. But without verbatim scripts, the Commission will not be able to ascertain whether BellSouth agents will comply with the equal access requirement. Furthermore, BellSouth does not offer any evidence that it has established any internal

(continued...)

to the script the Commission rejected in the Ameritech Michigan Order as "inconsistent on its face with our requirement that a BOC must provide the names of interexchange carriers in random order." Ameritech Michigan Order, ¶ 376. Indeed, to the extent the BellSouth script differs from the Ameritech script, it is even more objectionable, because it actively promotes BSLD service, while the Ameritech script simply identified the availability of Ameritech long distance service.

46. BellSouth has not even attempted to distinguish its proposed telemarketing practices from the practices the Commission rejected in the Ameritech Michigan Order, and instead simply argues that the Commission's Ameritech Michigan Order was wrong in this respect. BellSouth Br. at 63. Although BellSouth seeks reconsideration of the Commission's Order on marketing practices, BellSouth is obligated to comply with existing Commission requirements. See 47 U.S.C. § 405.

**VII. BELLSOUTH AND BSLD HAVE NOT PRESENTED ANY PLAN TO IDENTIFY AND CORRECT PAST DISCRIMINATION OR SUBSIDIZATION.**

47. When a BOC elects to provide in-region interLATA service through a pre-existing affiliate, as BellSouth has done, the BOC must present evidence to detail how it will identify, end, and correct, through a "true-up" or otherwise, all improper cross-subsidization and discrimination that may already have occurred prior to its application. The risk that such inappropriate subsidization or discrimination has occurred is substantial in this case, because BellSouth has admitted engaging in numerous transactions with BSLD and has stated that it has been operating to date under the view that none of the transactions between

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<sup>17</sup> (...continued)

procedures to monitor its agents' discussions with customers to ensure that equal access is enforced and that problems are expeditiously rectified.



it and BSLD have been subject to the restrictions of section 272 or the Accounting Safeguards Order. BellSouth Br. at 59.

48. BellSouth has not presented any evidence that it has established procedures to identify and correct any transactions that are not in compliance with section 272 and the Accounting Safeguards Order.<sup>18</sup> Unless BellSouth is called upon to identify and rectify any such past impermissible subsidies or transactions, BSLD would be able to enter the interLATA market with the very anticompetitive advantages that section 272 was designed to prevent. BellSouth has not even attempted to make such a showing.

**VIII. BELLSOUTH'S PAST COMPLIANCE DIFFICULTIES PROVIDE A SUBSTANTIAL BASIS TO DOUBT BELLSOUTH'S PAPER PROMISES TO COMPLY WITH SECTION 272.**

49. BellSouth has suggested that any section 272 compliance problems that it experiences will be uncovered and quickly rectified by either internal or external audits. See Cochran, ¶22; Jarvis at 4. BellSouth's recent compliance history, however, demonstrates that neither internal nor external audits will ensure that BellSouth will comply with section 272, and give substantial reason to doubt BellSouth's current paper promises of future compliance.

50. For example, the results of a joint federal and state audit of BellSouth's dealings with its affiliates<sup>19</sup> gives little reason to believe BellSouth's current claims that it

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<sup>18</sup> Even under BellSouth's view that it does not need to comply with section 272 until it receives interLATA authority, BellSouth Br. at 59, it currently must have procedures in place to identify and correct transactions that are not in compliance with section 272 and the Accounting Safeguards Order. Because BellSouth has not presented any evidence of such procedures, BellSouth has failed to meet its burden of proving that it will be in compliance with section 272 once it receives interLATA authority.

<sup>19</sup> Regional Audit of BellSouth and Certain Affiliated Companies, Dec. 17, 1993 ("Joint Audit").

will act in compliance with section 272. The Joint Audit, undertaken on behalf of the Commission and the National Association of Regulatory Utility Commissioners, "attempted to evaluate whether cross-subsidy exists between [BellSouth's] regulated and non-regulated operations."<sup>20</sup>

51. The audit team stated that BellSouth made it difficult for them to render an opinion regarding whether BellSouth was subsidizing nonregulated affiliates because of BellSouth's "consistent pattern of obstructionist behavior," which continued for at least eighteen months.<sup>21</sup> Furthermore, the audit team found that due to the lack of cooperation on the part of BellSouth that "many of the audit objectives were not fulfilled."<sup>22</sup> The results of the Joint Audit demonstrate that the Commission should give little weight to BellSouth's paper promises that 272 problems will be identified and quickly rectified by internal and external audits.

52. Similarly, in a related investigation of BellSouth's accounting practices, the Commission found numerous apparent violations by BellSouth of accounting rules and reporting requirements.<sup>23</sup> In particular, the Commission found that:

"The independent auditor's findings that we address here involve the misstatement or miscalculation of some \$6.2 million of interstate costs

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<sup>20</sup> Id. at 11 (Attachment 3).

<sup>21</sup> See id. ("obstructionist behavior" began in "May of 1992" and continued through at least December 1993).

<sup>22</sup> Id.

<sup>23</sup> In the Matter of the BellSouth Operating Companies, Order to Show Cause, 10 FCC Rcd 5637 (1995) ("Order to Show Cause") (Attachment 4). The Commission found numerous accounting irregularities including: (1) working capital violations; (2) jurisdictional separations violations; (3) misclassification of revenues; and (4) internal control failure including inadequate documentation to support accounting adjustments.

and revenues for the period from January 1988 through March 1989. . . . The seriousness of the misstatements is compounded here not only because of the net impact and the extent of understatements and overstatements, but also because of the scope and number of the errors or apparent violations, and the fact that they may have continued to the date of this Order to Show Cause. The findings reveal the BellSouth carriers' apparent failure to maintain their accounts, records, and memoranda in the manner prescribed by the Commission. To the extent that this conduct has continued, it must seriously undermine the Commission's confidence that BellSouth's accounts accurately reflect Commission-mandated accounting practices and reveal the true and lawful costs of BellSouth's interstate services."<sup>24</sup>

53. On November 1, 1996, the Commission issued a Consent Decree in which BellSouth agreed to appropriate corrective actions, including an independent audit of its internal accounting controls.<sup>25</sup> Even after the audit team returns its recommendations, BellSouth will have an additional six months before it takes any corrective action.<sup>26</sup> Consequently, BellSouth will have been able to delay fulfilling its legal obligation for over ten years from the date of the first uncovered violation. The results of this audit demonstrate that BellSouth's promises to quickly uncover and resolve 272 violations should be given little weight.

54. Moreover, it appears that BellSouth has already misused CPNI information to gain an unfair competitive advantage. Prior to switching the service of its customers who had selected a different local exchange carrier, BellSouth sent its customers a letter asking them to return to BellSouth's local service. Varner Aff., ¶ 234. BellSouth states that these letters mistakenly were sent as a result of a "programming change," yet it

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<sup>24</sup> Order to Show Cause at 5638 (emphasis added).

<sup>25</sup> In the Matter of the BellSouth Operating Companies, Consent Decree Order 11 FCC Rcd 14803 (1996) ("Consent Degree Order") (Attachment 5).

<sup>26</sup> Consent Degree Order at 14812.

did not catch this error for approximately six months, until August 1997. Id. Plainly, whatever internal oversight systems BellSouth had in place as recently as this past summer were ineffective in identifying and correcting this serious error. This example reinforces the concerns addressed in Section V regarding BellSouth's failure to bring forth any tangible evidence of procedures or systems in place to protect against section 272 violations.

55. This history shows BellSouth's willingness and ability to engage in obstructionist behavior to delay regulatory proceedings and judgements until its anticompetitive behavior has irrevocably altered the marketplace. Moreover, this history demonstrates that BellSouth's limited internal audit processes cannot be relied upon to promptly discover or rectify any problems that may emerge. The "past and present behavior of [BellSouth is] the best indicator of whether it will carry out the requested authorization in compliance with the requirements of section 272." Ameritech Michigan Order, ¶ 347. This past and present behavior demonstrate that until BellSouth brings forth tangible evidence of procedures or systems in place to protect against section 272 violations, the Commission cannot find that BellSouth will meet its obligations under section 272.

56. This concludes my affidavit.

I declare under penalty of perjury that the foregoing is true and accurate to the best of my knowledge and belief.

Executed on October 15<sup>th</sup>, 1997.

Patricia A. McFarland  
Patricia A. McFarland

SUBSCRIBED AND SWORN TO BEFORE ME this 15<sup>th</sup> day of October  
1997.

Richard Simone  
Notary Public

My Commission Expires:

**MY COMMISSION EXPIRES  
JANUARY 28, 2000**

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Section 272 (b)(5) of the Telecommunications Act of 1934 as amended by the Telecommunications Act 1996 requires that transactions between Section 272 affiliates and the Bell Operating Company of which they are an affiliate be "reduced to writing and available for public inspection." This index will contain a listing of those completed transactions between BellSouth Telecommunications, Inc. and BellSouth Long Distance, Inc. required to be posted on the internet by the Federal Communications Commission (FCC) in CC Docket 96-150. Required posting will occur within 10 days of the transaction.

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